



STATE BOARD OF EQUALIZATION

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July 8, 2010

Re: *Exclusion from Change in Ownership under Revenue and Taxation Code § 62(a)(2)*
Assignment No. 10-063

Dear Ms. :

This is in response to your letter dated April 8, 2010. You have asked our opinion on whether a change in ownership would occur upon the transfer of real property out of a limited liability company to one of its members who would then hold the property as a tenant in common with the limited liability company. It is our opinion that the property would not undergo a change in ownership under the facts you presented, and the remaining members would not become "original co-owners" with respect to their membership interests in the limited liability company.

Facts

A California limited liability company (the LLC) owns a parcel of real property in County (the Property). The members' membership interests in the LLC are in the percentages shown on the chart below.¹ The members are not original co-owners with respect to those interests.

It is proposed that Member A redeem its membership interest in exchange for an undivided interest in the Property equal to Member A's percentage membership interest in the LLC (the Transaction). The LLC will continue to own the remaining undivided interest in the Property as a tenant in common with Member A, and the remaining members of the LLC will indirectly own interests in the Property in the same respective proportions that they owned prior to the Transaction through their continued ownership of LLC membership interests.

¹ For property tax purposes, limited liability company membership interests are represented by the percentage of ownership in both capital and profits of the limited liability company. (See Property Tax Rule 462.180, subdivision (d)(1)(B), and Example 10. All "Rule" references herein are to sections of title 18 of the California Code of Regulations.)

BEFORE:**LLC capital and profits is owned:**

Member A	40%
Member B	15%
Member C	15%
Member D	15%
Member E	15%

The Property is owned:

LLC	100%
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AFTER:**LLC capital and profits is owned:**

Member B	25%
Member C	25%
Member D	25%
Member E	25%

The Property is owned:

LLC	60%
Member A	40%

Law & Analysis

In California, property may only be reassessed upon a change in ownership or upon the completion of new construction. (Cal. Const., Art. XIII A, § 2, subd. (a), Rev. & Tax. Code, § 110.1.)

Transfer of Undivided Tenancy in Common Interest

As a general rule, the transfer of any interest in real property to or from a legal entity is a change in ownership and results in a reappraisal of the property transferred. (Rev. & Tax. Code, § 61, subd. (j); Rule 462.180, subd. (a).) Section 62, subdivision (a)(2) provides an exclusion from change in ownership under section 61, subdivision (j) for transfers of real property between legal entities or between a legal entity and an individual. To qualify for the exclusion, such transfers must result solely in a change in the method of holding title to the real property, and the proportional ownership interests of the transferors and transferees in each and every piece of real property transferred must remain exactly the same both before and after the transfer.

Rule 462.180, subdivision (d)(4) extends the section 62, subdivision (a)(2) exclusion to transfers of interests in legal entities. Thus, transfers of legal entity interests between legal entities or between an individual and a legal entity which result solely in a change in the method of holding title, and in which proportional ownership interests in all real property represented by the transferred interests remain the same after the transfer, do not constitute a change in ownership.

In Property Tax Annotation 220.0454 (January 13, 2009), a legal entity transferred to a withdrawing owner that portion of its real property representing the withdrawing owner's proportionate share of entity ownership, in redemption of the owner's ownership interest in the entity. The other owner or owners continued to maintain their ownership of the real property indirectly through their entity ownership. We opined that the transfer to the withdrawing owner is excluded from change in ownership under section 62, subdivision (a)(2). Thus, under your facts, where the LLC transfers a 40 percent interest in the Property to Member A in exchange for Member A's interest in the LLC, the transfer is excluded from change in ownership.

Transfers of Membership Interests

Section 64, subdivision (a) provides the general rule that the transfer of ownership interests in a legal entity, such as limited liability company membership interests, does not constitute a transfer of the real property owned by the legal entity. There are exceptions to this general rule, contained in section 64, subdivisions (c)(1) and (d).

Under section 64, subdivision (c)(1), when any legal entity or individual obtains control through direct or indirect ownership or control of a majority ownership in any legal entity through the purchase or transfer of an ownership interest, that purchase or transfer causes a change in ownership of all of the real property owned by the entity. Section 64, subdivision (d), provides that when a transfer of real property is excluded from change in ownership under section 62, subdivision (a)(2), the holders of the legal entity interests immediately after the excluded transfer become "original co-owners" for purposes of determining the change in ownership consequences of any subsequent transfers of those legal entity interests. Subsequently, whenever ownership interests representing cumulatively more than 50 percent of the total interests in the legal entity are transferred by any of the original co-owners in one or more transactions, a change in ownership of that real property owned by the legal entity that was previously excluded from change in ownership under section 62, subdivision (a)(2) occurs.

As a result of Member A's complete withdrawal from the LLC, each remaining member's membership interest increased from 15 percent to 25 percent, which for property tax purposes is a deemed transfer to each such member of an additional percentage of LLC capital and profits. Under section 64, subdivision (a), such transfers do not constitute a transfer of the real property owned by the LLC. Because no member will obtain control of the LLC as a result of these transfers, the exception to section 64, subdivision (a) under section 64, subdivision (c)(1) for changes in control does not apply. In addition, because the members were not original co-owners with respect to their membership interests, section 64, subdivision (d) for cumulative transfers of original co-owner interests is inapplicable. Accordingly, the increases in the remaining members' membership interests do not result in a change in ownership of the Property.

Original Co-owner Status

The last issue is whether the remaining members would become original co-owners with respect to their membership interests. In Annotation 220.0454, under similar facts, we opined that the remaining partners of a limited partnership would become original co-owners with respect to their partnership interests. However, the facts in that situation were different in that the withdrawal of the partner caused a change in control of the partnership that would have resulted in a change in ownership of all of the partnership's property under section 64, subdivision (c)(1), unless an exclusion applied. Because there was an available exclusion under the proportional ownership interest exclusion (as extended to transfers of legal entity ownership interests under Rule 462.180, subdivision (d)(4)), the remaining partners became original co-owners under section 64, subdivision (d). Under your facts, because there was no change in control of the LLC as a result of Member A's withdrawal, there is no need to use the proportional ownership interest transfer exclusion with respect to the increase of the remaining members' membership interests, as discussed above, and thus the remaining members would not become original co-owners under section 64, subdivision (d). Accordingly, we find Annotation 220.0454 distinguishable on this point.

The views expressed in this letter are only advisory in nature; they represent the analysis of the legal staff of the Board based on present law and the facts set forth herein, and are not binding on any person or public entity.

Sincerely,

/s/ Matthew F. Burke

Matthew F. Burke
Tax Counsel III (Specialist)

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cc: Honorable
County Assessor

Mr. David Gau	MIC:63
Mr. Dean Kinnee	MIC:64
Mr. Todd Gilman	MIC:70